

STAFF REPORT
City Council Agenda
October 21, 2009

Date: October 13, 2009

To: Randy Mendosa, Interim City Manager

From: Mark Andre, Director, Environmental Services Department *MSA*

Re: Approve Agreement with PG&E, ClimateSmart Program Verified Emission Reduction Purchase and Sale Agreement

RECOMMENDATION

It is recommended that the City Council: Approve the Agreement with the PG&E ClimateSmart Program Verified Emission Reduction Purchase and Sale Agreement and Authorize the Interim City Manager to execute the necessary documents.

INTRODUCTION

On June 18, 2008, the City Council approved the submittal of a proposal to PG&E and authorized the Interim City Manager to sign the necessary application and solicitation agreement to market approximately 40,000 metric tons of verified carbon reduction (VER's) from the Arcata Community Forest (Sunny Brae and Barnum tracts).

The City's proposal was favorably received and staff has negotiated the final contract agreement and is now preparing to register the forest carbon reduction project with the Climate Reserve.

The ClimateSmart program is funded by PG&E customers in accordance with the California Public Utilities Commission. To make participating customers carbon neutral, PG&E enters into greenhouse gas (GHG) emission reduction contracts where the reductions occur over time into the future.

DISCUSSION

If approved, this would be the first ClimateSmart project with a local government agency as well as the first city in California to register a CO² reduction project on the Climate Registry. The project delivery period is 4 years and the verified carbon reduction is required to be maintained for at least 100 years.

This project has the potential to be replicated throughout the north coast region and beyond.

POLICY IMPLICATIONS

The project is consistent with the City's Greenhouse Gas Reduction Plan and the Standards and guidelines contained in the Arcata Community Forest/Jacoby Creek Forest Management Plan. The Forest Management Committee concurred with marketing verified carbon under the voluntary market. The project also furthers the City's model forest goal by providing leadership in the demonstration of sustainable forest management.

BUDGET/FISCAL IMPACT

The transaction results in a positive budgetary impact to the Forest Activity #87 which was budgeted during the budgetary process for the current fiscal year.

Attachments: Term Sheet.

Copies of the Agreement will be placed in the Council Attachment binder, lobby binder and agenda binders on Friday, October 16.

A copy of the City Proposal to PG&E dated June 18, 2009 is in the Council Mailbox

THIS SUMMARY OF TERMS IS FOR DISCUSSION PURPOSES ONLY. THERE IS NO OBLIGATION ON THE PART OF ANY NEGOTIATING PARTY UNTIL DEFINITIVE AGREEMENTS ARE SIGNED BY ALL PARTIES. THE TRANSACTIONS CONTEMPLATED BY THIS SUMMARY OF TERMS ARE SUBJECT TO THE SATISFACTORY COMPLETION OF DUE DILIGENCE AND NEGOTIATIONS. THIS SUMMARY OF TERMS DOES NOT CONSTITUTE EITHER AN OFFER TO SELL OR AN OFFER TO PURCHASE.

**ClimateSmart Purchase of Verified Emission Reductions
Term Sheet**

Seller	City of Arcata, Forestry Project
Buyer	Pacific Gas and Electric Company
Product	Buyer will purchase from Seller Verified Emission Reductions created and resulting from the Project ("VERs") pursuant to a form of VERs purchase agreement ("Agreement").
Project	Forestry project located in or near the City of Arcata in the State of California (the "Project") and is more fully described on Exhibit A attached hereto.
Amount of VERs during Delivery Term	40,000 total metric tons of VERs generated 10,000 metric tons per year in 2009 through 2012 to be delivered to Buyer ("Contracted VERs") in the following years: 2010 through 2013 ("Delivery Term").
Price	<p>The Price for the Contracted VERs shall begin at \$10.25/metric ton for VERs generated in 2009 and thereafter the Price shall increase on an annual basis by \$0.25/metric ton each year. ("Price").</p> <p>Buyer shall pay Seller for delivered VERs when the following are received:</p> <ul style="list-style-type: none"> • verification report, • evidence of the transfer in Climate Action Reserve ("CAR") database, • attestation, and • invoice for the VERs delivered. <p>Prepayment: Buyer to prepay \$50,000 ("Prepayment Amount") to Seller towards delivery of the Contracted VERs with the Prepayment Amount to be paid by Buyer within 20 business days of full execution of the Agreement. In connection with Prepayment Amount, Seller would agree to repay to Buyer the total Prepayment Amount by May 15, 2010 from Seller's revenue</p>

	<p>fund if Seller does not deliver at least 10,000 Contracted VERs by April 15, 2010. Between April 15, 2010 and May 15, 2010, the Prepayment Amount would accrue interest at the Interest Rate with such interest payable on May 15, 2010. If Seller does not repay the Prepayment Amount and all interest by May 15, 2010, Seller would be in default under the Agreement and the total aggregate amount of Prepayment Amount and prior accrued interest would accrue interest at the Interest Rate + 6% until repaid.</p> <p>“Interest Rate” means the rate per annum equal to the “Monthly” Federal Funds Rate (as reset on a monthly basis based on the latest month for which such rate is available) as reported in Federal Reserve Bank Publication H.15-519.</p>
<p>Excess VERs</p>	<p>If the Project produces more than the Contracted VERs during the Delivery Term or for any single year of the Delivery Term, Buyer will have the first right of refusal for any excess VERs from the Project.</p>
<p>Registration System</p>	<p>The initial registration system for the VERs shall be CAR.</p> <p><u>Replacement System</u>: If CAR is replaced by a new system, Seller shall pay the costs and expenses for registering with the new system during the Delivery Term.</p> <p><u>Additional System</u>: If a new registration system is created in addition to CAR or any replacement, Buyer may require Seller to register with such additional system upon Seller’s consent, which consent Seller shall not unreasonably withhold (if the additional system is required by a governmental entity, Seller’s consent shall not be required) and Buyer shall reimburse Seller for the costs and expenses associated with such registration.</p>
<p>Milestones</p>	<ul style="list-style-type: none"> • Project Start Date: January 1, 2009. “Project Start date: means Seller has modified its operation to begin creating Contracted VERs. • Project Listed with CAR: by November 30, 2009. “Project Listed with CAR” means Project Submittal Form provided to and accepted by CAR. • Project Registered with CAR: by January 1, 2010. “Project Registered with CAR” means Seller has submitted the final Verification Report to CAR. • Project Verification Report Delivered to CAR: by February 15, 2010. “Project Verification Report Delivered to CAR” means that Seller has submitted initial verification report to CAR and Seller reasonably expects CAR to accept such report and issue serial numbers for the VERs that are the subject of the verification report.

	The above milestones are "Guaranteed Milestones". Following the Project Verification Delivered to CAR, Seller shall use diligent efforts to obtain the final verification from CAR for the VERs that are the subject of the verification report. If CAR does not accept the final verification report and has not issued serial numbers for the VERs that are the subject of the accepted verification report by May 15, 2010, Buyer may terminate the Agreement.
Additionality	<p>Seller shall meet all the Climate Action Reserve ("CAR") Protocols and PG&E ClimateSmart Program RFP requirements for additionality.</p> <p><u>Baseline</u>: Seller shall establish and report a baseline for the Project.</p> <p><u>Regulatory</u>: As required by CAR Protocols, if Seller is required by statute or regulation to engage in the activity then the Project is not additional ("Regulatory Additionality").</p> <p><u>Financial</u>: As required by the ClimateSmart Program, Seller must demonstrate financial additionality, such that the Project would have a lower than acceptable rate of return for Seller and would not have happened without Buyer's payment of price for the VERs.</p>
Leakage	Upon execution of the contract and during the Delivery Term (2010 through 2013), Seller will not engage in activity shifting leakage activities on its forest property. Activity-shifting leakage is the displacement of activities from inside the Project's physical boundaries to locations outside of the Project's boundaries as a direct result of the Project, causing an increase in emissions outside of the Project's physical boundaries. In other words, Seller cannot compensate for the more limited harvest due to the Project by shifting the harvest to another property area outside of the Project boundaries but within entity boundaries.
Exclusive Ownership of VERs	Seller shall provide to Buyer acknowledgments from all persons connected with the Project or shall otherwise provide evidence satisfactory to Buyer to establish exclusive ownership of the VERs. Buyer will have a first priority security interest in all VERs to be delivered by Seller throughout the term of the agreement. The VERs shall be transferred to Buyer free and clear of all liens, rights and claims of any other party.
Progress Reports and Other Reporting	<ul style="list-style-type: none"> • Monthly Progress Reports from execution of the contract and prior to Project Verified by CAR • Annual Progress Reports during Delivery Term on February 15 of each year. • General maintenance of and Buyer right to review

	<p>records.</p> <ul style="list-style-type: none"> • Financial Reporting of Seller to Buyer which reporting may be satisfied by directing Buyer to Seller's annual public financial reporting • Buyer premises and project inspection rights subject to reasonable restrictions and notification.
<p>Performance Excuses</p>	<p>Seller shall be excused from delivering the VERs only:</p> <ul style="list-style-type: none"> • during a Force Majeure Event, or • by Buyer's failure to perform. <p>Buyer shall be excused from receiving or paying for VERs only:</p> <ul style="list-style-type: none"> • during a Force Majeure Event, or • by Seller's failure to perform.
<p>Force Majeure</p>	<p>Force Majeure means any event or circumstance which wholly or partly prevents or delays the performance of any material obligation arising hereunder, but only if and to the extent:</p> <ul style="list-style-type: none"> • such event is not within the reasonable control, directly or indirectly, of the Party seeking to have its performance obligations excused thereby, • the Party seeking to have its performance obligations excused thereby has taken all reasonable precautions and measures in order to prevent or avoid such event or mitigate the effect of such event on such Party's ability to perform its obligations hereunder and which by the exercise of due diligence such Party could not reasonably have been expected to avoid and which by the exercise of due diligence it has been unable to overcome, and • such event is not the direct or indirect result of the negligence or the failure of, or caused by, the Party seeking to have its performance obligations excused thereby. Subject to the foregoing, events that could qualify as Force Majeure include earthquake, explosion, or other catastrophic event not related to or enhanced by climate change; or war (declared or undeclared), riot or similar civil disturbance, acts of the public enemy (including acts of terrorism), sabotage, blockage, insurrection, revolution, expropriation or confiscation; <p>provided, however, that Force Majeure may <i>not</i> be based on:</p> <ul style="list-style-type: none"> • Seller's ability to sell the Contracted VERs for more than the Price; • Seller's inability to obtain approvals of any type for the operation or maintenance of the Project, unless such

	<p>delay is directly attributable to the failure of CAR;</p> <ul style="list-style-type: none"> • forest fire, insect infestation or disease affecting trees, plants or livestock, no matter how pervasive or destructive; • Seller’s failure to obtain additional funds, including funds authorized by a state or the federal government or agencies thereof, to supplement the Price for the Contracted VERs; • a strike, work stoppage or labor dispute limited only to any one or more of Seller, Seller’s Affiliates, or any contractor or subcontractor thereof or any other third party employed by Seller to work on the Project; • a general increase in prevailing regional wages.
<p>Events of Default</p>	<p>An “Event of Default” shall be as provided in the Agreement, which in general provides,</p> <p>(1) With respect to Seller as the defaulting party, the occurrence of any of the following:</p> <ul style="list-style-type: none"> • failure to deliver VERs • failure to maintain Project • non-compliance with the CAR-compliant project monitoring and verification methodologies of Seller and the approved verifier does not reasonably believe that compliance can be obtained, • delivery of committed VERs to another party, • failure to achieve a Guaranteed Milestone, • foreclosure of Project or Premises, • Seller causes a material adverse effect on Buyer or its affiliates, or • Seller intentionally interferes with approved verifier’s work or provides false information. <p>(2) With respect to both parties, the occurrence of any of the following:</p> <ul style="list-style-type: none"> • failure to make payments, • breach of a representation or warranty, • failure to perform a material covenant, • bankruptcy, or • consolidation or merger of a party without assumption of all obligations. <p>Both parties shall be provided with reasonable time periods and mechanisms to cure defaults.</p>
<p>Seller Compliance with</p>	<p>To insure the eligibility of the VERs, Seller agrees to:</p>

<p>CAR Protocols</p>	<ul style="list-style-type: none"> • Comply with the CAR Protocols, • Register Seller with Climate Action Reserve (CAR), • Project Listed with CAR, • Maintain registrations during the Delivery Term, and • Obtain and pay for the Initial Verification Report, Project Certification, Certification and each Verification Report according to the Approved Methodologies.
<p>Remedies</p>	<p><u>Replacement VERs</u>: If a Seller Event of Default causes a loss of VERs delivered, or a shortfall of VERs to be delivered to Buyer (“Lost VERs Event”), Seller shall replace any such VERs with VERs with a 2009 vintage or later, registered with CAR (“Replacement VERs”) in the following order of preference:</p> <ul style="list-style-type: none"> • From the Project; • From same type of project managed or owned by Seller in California; • From same type of project in California; or • Other VERs generated in California. <p><u>Refund</u>: If a Lost VERs Event occurs and there are no Replacement VERs available for Seller’s purchase and delivery as provided above, Seller shall refund all payments for the affected VERs.</p> <p><u>Damages</u>: In the event of a default by Seller, Seller shall be liable for Buyer’s contracting costs and Buyer’s cover damages, which are the difference between the Price and the cost to Buyer of purchasing VERs meeting the CAR and the PG&E ClimateSmart Program requirements.</p> <p>In the event of default by Buyer, Seller may terminate the contract, and Seller shall be relieved of obligations to Buyer under this contract, provided that Seller is not also in default.</p> <p><u>Step-In Rights</u>: If the VERs have been generated from the Project, but Seller fails or refuses to verify the VERs and is in default under the Agreement and Buyer is not in default under the terms of the agreement, then Buyer may engage an Approved Verifier to perform such verification and Seller shall provide access to the Project for such verification.</p>
<p>Reserve</p>	<p>In order to provide Buyer with assurances in the event of a Lost VERs Event, Seller shall have reserved VERs in the CAR buffer pool. The Amount of VER’s contributed to the buffer pool shall be determined pursuant to Version 3.0 of CAR Forest Project Protocol Appendix C.</p>
<p>Insurance</p>	<p>Seller shall maintain the following types insurance coverage pursuant to its self insurance and be responsible for its contractors or subcontractors maintaining sufficient limits of the appropriate</p>

	<p>insurance coverage:</p> <ul style="list-style-type: none"> • Workers' Compensation and Employer's Liability; • Commercial General Liability; and • Auto
Right to Terminate Agreement	<p>Buyer has the right to terminate the Agreement without liability to either party if:</p> <ul style="list-style-type: none"> • A Force Majeure Event prevents Seller from meeting a Guaranteed Milestone or delivering 50% of the annual amounts in two consecutive years during the Delivery Term, • Regulatory Additionality for the Project no longer exists; or • Seller does not have its initial verification report accepted by CAR and serial numbers for the VERs that are the subject of such report issued by CAR, by May 15, 2010. <p>Seller may also terminate the Agreement without liability if Regulatory Additionality for the Project no longer exists.</p> <p>See also Damages under Remedies section above.</p>
Promotion	<p>The Parties shall coordinate talking points with respect to the Project for oral public announcements and each Party shall have a reasonable opportunity to review and approve written announcements, disclosures, advertising or promotional materials.</p>
CAR Protocol	<p>Means version 3.0 of the Forest Project Protocol was approved by CAR September 1, 2009.</p>

EXHIBIT A

PROJECT DESCRIPTION

The Project will take place within two City of Arcata forest holdings, the Barnum tract of the Jacoby Creek Forest and the Sunny Brae Forest. The forest management activities comprising the Project will not occur on the entire forest area of the two forests and a more complete description of the Project and Premises can be found below.

The Delivery Term will be from 2009-2012, with Seller selling and delivering VERs to Buyer in 2010, 2011, 2012, and 2013 pursuant to the Agreement. The proposed amount of VERs to be sold and delivered to Buyer is 10,000 each year for a total of 40,000 VERs by the end of the Delivery Term.

The Premise:1. 'Barnum' tract of the Jacoby Creek Forest

The 'Barnum' tract of the Jacoby Creek Forest consists of two legal parcels tallying 285 acres. The Barnum tract is located in unincorporated Humboldt County, south of Arcata, north of Eureka, and east of the US Highway 101. The following is a general description of the location of the Barnum tract, not including the more specific easements and private properties within the area.

Barnum tract described as follows:Parcel one:

Portions of Section 24, Township 5 North, Range 1 East, Humboldt Meridian

All in Section 24, Township 5 North, Range 1 East, Humboldt Meridian, excepting easements and private holdings

Lot 3 in Section 19, Township 5 North, Range 2 East, Humboldt Meridian

Portions of Section 24, Township 5 North, Range 1 East, Humboldt Meridian

Lot 4 of Section 19, Township 5 North, Range 2 East, Humboldt Meridian

Parcel two:

Portions of section 24, Township 5 North, Range 1 East, Humboldt Meridian

2. Sunny Brae Forest

The Sunny Brae Forest is 175 acres located northwest of the Barnum tract area, just east of the Sunny Brae neighborhood in southern Arcata.

Sunny Brae Forest described as follows: Section 34 in Township 6 North, Range 1 East, Humboldt Meridian: The East Half of the Southwest Quarter and the South Half of the Southeast Quarter.

The Project:

The Project will consist of forest management activities consistent with CAR Protocol on the Premises during the Delivery Term. The activities comprising the Project will not occur on the entire Premises.